

FRANCHISE AND EXCISE TAX

The **Franchise Tax** is based on values shown on a company's balance sheet at the end of its fiscal year. The franchise tax rate of 25 cents per \$100 is applied to the net worth, or the book value, of property, whichever is greater. The franchise tax on a return may be prorated only if: 1) a domestic taxpayer closes its tax year less than 12 months from Tennessee incorporation; 2) a foreign taxpayer closes its tax year less than 12 months from beginning business in Tennessee; or 3) a taxpayer changes its accounting period for federal tax purposes so that a return covering a tax year of less than 12 months is required. The franchise tax may not be prorated on short-period returns resulting from a taxpayer merging out of existence into another entity or short-period returns resulting from dissolutions.

Net worth is defined as total assets less total liabilities, determined in accordance with generally accepted accounting principles. Taxpayers, except unitary groups filing on a combined basis, who do not keep their books and records using generally accepted accounting principles to compute net worth may use the same method used for federal income tax purposes, as long as such method fairly reflects the taxpayer's net worth for purposes of the franchise tax.

The **Excise Tax** is imposed on the net earnings derived from business conducted in Tennessee, as reported on the profit and loss statement. A tax rate of 6.5% is applied to the net earnings for the fiscal year. For excise tax purposes, "net earnings" is defined as federal taxable income before the net operating loss deduction and special deductions subject to certain state adjustments. Examples of some of the adjustments are: (1) Tennessee excise tax deducted on the federal return is not allowed for state purposes, (2) charitable contributions made during the fiscal year are deductible for state purposes with no limit on the amount, except that the fair market value of property donated cannot exceed the actual cost of such property, and (3) any qualifying net operating loss incurred while subject to excise tax in previous years may be deducted. Any qualifying net operating loss incurred for fiscal years ending on or after 1/15/84 may be carried forward for 15 years.

For S Corporations, "pass through" income is added back to net earnings and "pass through" expense items on Federal Schedule K, Form 1120S are deducted. Because Tennessee does not recognize the federal "S" status election, an S Corporation files as though it had not elected "S" status.

To the extent that the deduction does not create a loss, an entity that is treated as a partnership for federal income tax purposes or that is required to file a federal form 1065 partnership return or variation thereof, including, but not limited to, a limited liability company, may deduct the amount subject to self-employment taxes distributable or paid to each partner or member, without regard to any cap, and may deduct amounts contributed to a qualified pension or benefit plan when computing its net earnings for Tennessee excise tax purposes. A limited liability company that is included in the federal form 1040 filed for federal income tax purposes by its single member who is a natural person may also take such a deduction.

A taxpayer who is a member of an entity filing a Federal Form 1065 will adjust net earnings by deducting the "pass through" income and adding back the "pass through" expenses reported on the federal return, if received from an entity subject to Tennessee franchise and excise tax.

The gain or loss on an asset distributed by a partnership, S Corporation, or business trust within 12 months of sale to a member, partner, shareholder, or certificate holder is included in the tax base.

Quarterly Estimated Payments of franchise and excise tax are required if the combined liability for the current year is \$5,000 or more. The minimum quarterly payment is the lesser of: (a) 25% of the prior year's combined Franchise and Excise Tax liability, or (b) 25% of 100% of the current year's combined liability.

Due Dates – A schedule of due dates for the return, extension, and estimated payments, based on the fiscal year end, is as follows:

Beginning 7/1/05							
Fiscal Year		Due Date of Return	6 Month Ext. Due Date	Estimated Franchise & Excise Tax Payments			
Beginning	Ending			1st	2nd	3rd	4th
07/01/2005	06/30/2006	10/15/2006	04/15/2007	10/15/2005	12/15/2005	03/15/2006	07/15/2006
08/01/2005	07/31/2006	11/15/2006	05/15/2007	11/15/2005	01/15/2006	04/15/2006	08/15/2006
09/01/2005	08/31/2006	12/15/2006	06/15/2007	12/15/2005	02/15/2006	05/15/2006	09/15/2006
10/01/2005	09/30/2006	01/15/2007	07/15/2007	01/15/2006	03/15/2006	06/15/2006	10/15/2006
11/01/2005	10/31/2006	02/15/2007	08/15/2007	02/15/2006	04/15/2006	07/15/2006	11/15/2006
12/01/2005	11/30/2006	03/15/2007	09/15/2007	03/15/2006	05/15/2006	08/15/2006	12/15/2006
01/01/2006	12/31/2006	04/15/2007	10/15/2007	04/15/2006	06/15/2006	09/15/2006	01/15/2007
02/01/2006	01/31/2007	05/15/2007	11/15/2007	05/15/2006	07/15/2006	10/15/2006	02/15/2007
03/01/2006	02/28/2007	06/15/2007	12/15/2007	06/15/2006	08/15/2006	11/15/2006	03/15/2007
04/01/2006	03/31/2007	07/15/2007	01/15/2008	07/15/2006	09/15/2006	12/15/2006	04/15/2007
05/01/2006	04/30/2007	08/15/2007	02/15/2008	08/15/2006	10/15/2006	01/15/2007	05/15/2007
06/01/2006	05/31/2007	09/15/2007	03/15/2008	09/15/2006	11/15/2006	02/15/2007	06/15/2007

If you have questions regarding the franchise and excise tax laws or wish to request forms, please contact the Tennessee Department of Revenue at (800) 397-8395 for in-state taxpayers and (615) 253-0700 for Nashville and out-of-state taxpayers. You may also contact the department by e-mail at tn.revenue@mail.state.tn.us, or you may visit our Web site at www.Tennessee.gov/revenue.

